WEEKLY COMMENTARY

What More Could They Ask For?

By Royce Mendes, Managing Director and Head of Macro Strategy

There's ample evidence that the Bank of Canada's interest rate increases are working exactly as intended. Consumers have reined in their spending. Businesses are barely hiring. And inflation has fallen just about as fast as it rose. So it's fair for Canadians to ask why they aren't getting any relief on interest rates just yet.

It's true that the economy eked out slightly more growth than analysts expected in the final trimester of 2023. It's also true that GDP growth is beginning the year on stronger footing than the Bank of Canada anticipated. But the numbers are hardly worth celebrating.

The economy's performance in both the fourth quarter of last year and the first quarter of this year are uninspiring. Roughly 1% growth isn't anything to write home about, particularly given the surge in population growth.

The expansion that occurred towards the end of 2023 also had nothing to do with activity within our nation's borders. In fact, final domestic demand contracted for the first time since 2022. Moreover, much of the increase in economic activity that's been seen early this year is attributable to labour disputes ending in Quebec. That's a one-time boost to the economy, not sustainable growth.

In any other time over the past thirty years, central bankers would have been openly discussing the need to ease policy. So far this year, however, they've been tight lipped. Their rationale is that underlying inflation remains sticky above the 2% target, so the time for rate cuts is off in the distance.

The problem is that the central bank has been relying too heavily on its two preferred metrics of core inflation: CPI-median and CPI-trim. While policymakers claim they have been looking at a broad suite of inflation indicators, other measures showed much more progress towards the Bank of Canada target at the time of the last Monetary Policy Report.

Fast forward six weeks and inflationary pressures look even tamer. The Bank of Canada's former favourite measure of core inflation, CPIX, now sits at just 2.4% on a year-over-year basis. Inflation excluding shelter is all the way down to 1.6%. So, although both CPI-median and CPI-trim remain comfortably above 3%, using a wider lens to look at inflation indicators would suggest much more muted price growth.

It's important that central bankers calibrate their response functions to the right inflation measure. High interest rates are doing more damage than just cooling off an overheated economy. Elevated borrowing costs are causing developers to pause or cancel homebuilding projects, further exacerbating the housing supply shortages in this country. Businesses are also curtailing investment activity, making it even more difficult to generate productivity growth.

Our assumption is that the Bank of Canada will sound more dovish next week. It's clear that the domestic economy is struggling, with commercial banks reporting more borrowers having trouble with loan repayments. Wages also might not be growing as fast as previously believed. New payroll data released this week showed wage growth of just 2.4%, roughly half of the 4% to 5% increase the Bank of Canada cited back in January. Most importantly, however, central bankers will need to acknowledge the progress made in containing inflation.

While underlying inflationary pressures are probably still slightly above target, it's time to take a more nuanced approach to describing price growth. In doing so, the central bank will begin opening the door ever so slightly to potential rate cuts.

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Desjardins Economic Studies: 514-281-2336 or 1-866-866-7000, ext. 5552336 • desjardins.economics@desjardins.com • desjardins.com/economics

NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.

Our base case is that the Bank of Canada will begin lowering rates in June. However, should the upcoming employment readings disappoint or inflation numbers cool off more quickly than we expect, it's possible that the central bank starts moving as early as April. Because really, what more could they ask for?

What to Watch For

By Randall Bartlett, Senior Director of Canadian Economics, Tiago Figueiredo, Associate – Macro Strategy, Marc Desormeaux, Principal Economist, Marc-Antoine Dumont, Senior Economist, and Francis Généreux, Principal Economist

UNITED STATES

TUESDAY March 5 - 10:00	
February	
Consensus	52.9
Desjardins	52.6
January	**53.4**

ISM Services index (February) – After an alarming drop in December, the ISM Services index rebounded to 53.4 in January, the highest it's been since September 2023. But we believe that rather than continuing its climb in February, the index probably dipped slightly. Regional non-manufacturing indexes offered mixed readings in February, as did the major consumer confidence indexes. Consequently, the ISM Services index is expected to have slid to 52.6, which is still above the threshold for economic growth.

THURSDAY March 7 - 15:00	
January	**US$B**
Consensus	10.000
Desjardins	15.000
December	**1.561**

Consumer credit (January) – Consumer credit growth slowed sharply in December. It expanded by US$1.6 billion, in stark contrast to the average gain of US$16.5 billion over the preceding three months. It'll be interesting to see if the pullback continued in January. A cooldown in consumer spending and a slight uptick in the savings rate suggest another month of lacklustre credit growth. But weekly data on bank credit point to a recovery. All things considered, we expect credit to have expanded by around US$15 billion.

FRIDAY March 8 - 8:30	
February	
Consensus	190,000
Desjardins	200,000
January	**353,000**

Change in nonfarm payrolls (February) – US job market growth remains surprisingly strong. In January, net hires came in above 300,000 for the second month in a row. In February, the expectation is, once more, for hiring to have slowed. It remains to be seen whether forecasters will be proven wrong yet again. The components related to the job market in the Conference Board's Consumer Confidence Index fell slightly in February. But regional business surveys provided mixed data on changes in the number of employees from January to February. That said, weekly initial unemployment claims dropped sharply in the week that the establishment survey was conducted. We believe around 200,000 new jobs were added in February, while unemployment probably rose to 3.8%. We'll need to keep an eye on changes in hours worked and average hourly wages, which were influenced by bad weather in January.

CANADA

WEDNESDAY March 6 - 9:45	
March	
Consensus	5.00%
Desjardins	5.00%
January 24	**5.00%**

Bank of Canada meeting (March) – The Bank of Canada will leave interest rates on hold on March 6, but is likely to sound at least somewhat more dovish relative to the January rate announcement. While GDP data have modestly exceeded the central bank's projections, the details show that the domestic economy is anything but healthy. Most importantly, inflation has cooled more than the Bank of Canada's forecast. That should allow policymakers to present a more balanced statement. We continue to expect the central bank will begin lowering rates in June, with five 25bp rate cuts penciled in for this year.

THURSDAY March 7 - 8:30	
January	**$B**
Consensus	0.29
Desjardins	-0.60
December	**-0.31**

International trade (January) – Canada's merchandise trade balance is expected to have slid further into negative territory. We anticipate that an increase in imports was the main driver behind this decline, as inputs to our forecast suggest that imports of motor vehicles and parts edged up in January. Furthermore, the depreciation of the Canadian dollar is likely to have pushed up import prices. On the export side, we expect a relatively flat read for January. Month-over-month, seasonally adjusted oil prices were down 4.4 % in the first month of the year, weighing on exports. That said, the brand-new Trans Mountain oil pipeline should come online this spring, which should support higher exports in the second half of 2024.

FRIDAY March 8 - 8:30	
February	
Consensus	21,400
Desjardins	5,000
January	**37,300**

Net change in employment (February) – Canada's employment indicators are beginning to tell different stories. According to the Labour Force Survey, the economy created jobs in each of the past three months. However, the more reliable but less timely payroll data suggest that employment declined during the same period. That's true even after accounting for labour disputes. While we're not going to pencil in a negative number for the net change in employment for February, a soft 5K gain would still push the unemployment rate up two ticks to 5.9%. According to the Labour Force Survey, wage growth has also been strong, in contrast to the weak numbers seen in the payroll data. We expect the Labour Force Survey numbers will begin to decelerate in the months to come.

OVERSEAS

THURSDAY March 7 - 8:15	
March	
Consensus	4.50%
Desjardins	4.50%
January 25	**4.50%**

Eurozone: European Central Bank meeting (March) – It's still too early for the ECB to start cutting rates, but we think the time is coming. The central bank may give us a better idea of what it's planning at next week's meeting, especially since it will have new economic and inflation forecasts to share. Inflation fell rapidly in the last quarter of 2023. Unfortunately, February's strong rebound in CPI excluding food and energy adds noise on the line. But with economic growth currently close to 0%, the chances of hitting the inflation target in the foreseeable future still seem good. We expect a first interest rate cut in the eurozone in June.

FRIDAY March 8 - 20:30	
February	**y/y**
Consensus	0.2%
January	**-0.8%**

China: Consumer price index (February) – China experienced a fourth straight month of deflation in January, with the consumer price index down 0.8% year-on-year. This came on the heels of yearly declines of 0.2%, 0.5% and 0.3% in October, November and December 2023. The main source of deflationary pressures was meat, with a combination of abundant supply and sluggish demand sending prices plummeting. But prices for services, including tourism, picked up as part of the post-COVID rebound, which came a little later in China. Expansionary fiscal policy and the central bank's recent interest rate cut raise hopes that inflation could eventually head back above zero. The February print will tell us more about the extent of the deflation problem in China.

Economic Indicators

Week of March 4 to 8, 2024

Day	Time	Indicator	Period	Consensus	Desjardins	Previous reading
UNITED STATES						
MONDAY 4	11:00	Speech by Federal Reserve Bank of Philadelphia President P. Harker				
TUESDAY 5	10:00	ISM Services index	Feb.	52.9	52.6	53.4
	10:00	Factory orders (m/m)	Jan.	-3.0%	-2.5%	0.2%
WEDNESDAY 6	10:00	Wholesale inventories – final (m/m)	Jan.	n/a	-0.1%	-0.1%
	10:00	Testimony of Federal Reserve Chair J. Powell before a Congressional committee				
	12:00	Speech by Federal Reserve Bank of San Francisco President M. Daly				
	14:00	Release of the Beige Book				
THURSDAY 7	8:30	Initial unemployment claims	Feb. 26–March 1	n/a	213,000	215,000
	8:30	Trade balance – goods and services (US$B)	Jan.	-63.2	-64.0	-62.2
	8:30	Nonfarm productivity – final (ann. rate)	Q4	3.1%	3.1%	3.2%
	8:30	Unit labor costs – final (ann. rate)	Q4	0.7%	0.6%	0.5%
	10:00	Testimony of Federal Reserve Chair J. Powell before a Congressional committee				
	11:30	Speech by Federal Reserve Bank of Cleveland President L. Mester				
	15:00	Consumer credit (US$B)	Jan.	10.000	15.000	1.561
FRIDAY 8	7:00	Speech by Federal Reserve Bank of New York President J. Williams				
	8:30	Change in nonfarm payrolls	Feb.	190,000	200,000	353,000
	8:30	Unemployment rate	Feb.	3.7%	3.8%	3.7%
	8:30	Average hourly earnings (m/m)	Feb.	0.2%	0.1%	0.6%
	8:30	Average weekly hours	Feb.	34.3	34.3	34.1
CANADA						
MONDAY 4	---	---				
TUESDAY 5	---	---				
WEDNESDAY 6	8:30	Labour productivity (q/q)	Q4	-0.1%	0.5%	-0.8%
	9:45	Bank of Canada meeting	March	5.00%	5.00%	5.00%
	10:30	Speech by Bank of Canada Governor T. Macklem and Senior Deputy Governor C. Rogers				
THURSDAY 7	8:30	Building permits (m/m)	Jan.	n/a	6.9%	-14.0%
	8:30	International trade ($B)	Jan.	0.29	-0.60	-0.31
FRIDAY 8	8:30	Net change in employment	Feb.	21,400	5,000	37,300
	8:30	Unemployment rate	Feb.	5.8%	5.9%	5.7%
	8:30	Industrial capacity utilization rate	Q4	n/a	81.9%	79.7%

NOTE: Each week, Desjardins Economic Studies takes part in the Bloomberg survey for Canada and the United States. Approximately 15 economists are consulted for the Canadian survey and a hundred or so for the United States. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Following the quarter, the abbreviations f, s and t correspond to first estimate, second estimate and third estimate respectively. Times shown are Eastern Standard Time (GMT - 5 hours). Desjardins Economic Studies forecast.

Economic Indicators

Week of March 4 to 8, 2024

Country	Time	Indicator	Period	Consensus m/m (q/q)	Consensus y/y	Previous reading m/m (q/q)	Previous reading y/y
OVERSEAS							
DURING THE WEEK							
China	---	Trade balance (US$B)	Feb.	n/a		103.79	
MONDAY 4							
Japan	18:30	Tokyo Consumer Price Index	Feb.	2.5%		1.8%	
Japan	19:30	Composite PMI – final	Feb.	n/a		50.3	
Japan	19:30	Services PMI – final	Feb.	n/a		52.5	
TUESDAY 5							
France	2:45	Industrial production	Jan.	0.0%	1.7%	1.1%	0.9%
Italy	3:45	Composite PMI	Feb.	51.5		50.7	
Italy	3:45	Services PMI	Feb.	52.3		51.2	
France	3:50	Composite PMI – final	Feb.	47.7		47.7	
France	3:50	Services PMI – final	Feb.	48.0		48.0	
Germany	3:55	Composite PMI – final	Feb.	46.1		46.1	
Germany	3:55	Services PMI – final	Feb.	48.2		48.2	
Italy	4:00	Real GDP – final	Q4	0.2%	0.5%	0.2%	0.5%
Eurozone	4:00	Composite PMI – final	Feb.	48.9		48.9	
Eurozone	4:00	Services PMI – final	Feb.	50.0		50.0	
United Kingdom	4:30	Composite PMI – final	Feb.	53.3		53.3	
United Kingdom	4:30	Services PMI – final	Feb.	54.3		54.3	
Eurozone	5:00	Producer price index	Jan.	-0.1%	-0.8%	-0.8%	-10.6%
WEDNESDAY 6							
Germany	2:00	Trade balance (€B)	Jan.	21.0		22.4	
United Kingdom	4:30	Construction PMI	Feb.	49.0		48.8	
Eurozone	5:00	Retail sales		0.1%	-1.3%	-1.1%	-0.8%
THURSDAY 7							
Germany	2:00	Factory orders	Jan.	-6.5%	-5.5%	8.9%	2.7%
Eurozone	8:15	European Central Bank meeting	March	4.50%		4.50%	
Japan	18:50	Current account (¥B)	Jan.	2,074.4		1,810.0	
FRIDAY 8							
Japan	0:00	Leading indicator – preliminary	Jan.	109.7		110.2	
Japan	0:00	Coincident index – preliminary	Jan.	110.2		115.9	
Germany	2:00	Producer price index	Jan.	0.1%	-6.8%	-1.2%	-8.6%
Germany	2:00	Industrial production	Jan.	0.6%	-5.0%	-1.6%	-3.0%
France	2:45	Trade balance (€M)	Jan.	n/a		-6,829	
France	2:45	Current account (€B)	Jan.	n/a		-0.7	
Eurozone	5:00	Real GDP – final	Q4	0.0%	0.1%	0.0%	0.1%
Eurozone	5:00	Net change in employment – final	Q4	n/a	n/a	0.3%	1.3%
China	0:00	Producer price index	Feb.		-2.6%		-2.5%
China	0:00	Consumer price index	Feb.		0.2%		-0.8%

NOTE: Unlike release times for US and Canadian economic data, release times for overseas economic data are approximate. Publication dates are provided for information only. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Times shown are Eastern Standard Time (GMT - 5 hours).